2022-23 ANNUAL REPORT

FARM CREDIT CANADA

Agriculture industry overview

FCC monitors important factors that influence the short- and long-term prospects, profitability, and financial health of the agriculture and agri-food industry.

The Canadian agriculture and agri-food industry experienced several disruptions in 2022 due to the war in Ukraine, extreme weather and labour availability. These disruptions affected input availability and increased prices, wages and interest rates, causing many businesses to become less optimistic about the future. Despite the market turmoil, however, the agriculture and agri-food industry performed much better than the Canadian economy as a whole, while agri-food manufacturing experienced more challenges. Agriculture, forestry, fishing and hunting GDP increased 10.5% in 2022, while agri-food manufacturing increased 2.8%, compared with a 3.6% increase for the overall economy.

Russia's invasion of Ukraine and the economic sanctions imposed on Russia caused significant global market uncertainty, most notably for energy and agriculture commodities. For the Canadian agriculture and agri-food industry, the result was increased prices of crop inputs and fuel. This also created challenges for sourcing fertilizer. However, the uncertainty also supported higher prices for grains and oilseeds.

Farm cash receipts increased 13.6% in 2022 as higher production in Eastern Canada as well as higher prices for agriculture commodities offset limited grain supply in Western Canada because of the 2021 drought. Food and beverage manufacturing revenues also expanded, increasing 11%, largely as a result of higher prices because volume growth was limited.

Farm and manufacturing revenues increased on higher prices

In 2022, total Canadian crop production increased 34% to 96.0 million tonnes, recovering from the 2021 drought conditions that impacted the prairies. Good yields across Canada and historically strong commodity prices supported crop receipts. As a result, most operations were able to absorb the high input costs in 2022. Avian influenza was prevalent in 2022 and is expected to continue into 2023. While the beef herd continued to contract in Canada, 2022 did see a return to normal hay crops and strong pricing opportunities for cattle. Overall crop receipts increased 14.2% and livestock receipts increased 12.5% in 2022. Cash receipts from government direct payments were also up 14.0% as western producers received crop insurance from the 2021 crop.

Farm input prices rose significantly in 2022 compared to 2021. Fertilizer prices rose 87% on average due to a combination of higher energy prices and global fertilizer production constraints. Fuel prices also rose significantly in 2022, with farm diesel rising 44% and farm gasoline 27%. Commercial seed and pesticides increased on average 13.8% and 15%, respectively, in 2022 due to a combination of reduced availability of seed from the 2021 drought, higher energy prices and global supply constraints on chemical manufacturing. Farm input inflation resulted in 2022 being the most expensive crop ever planted. Average input prices for animal production increased 30% due to significantly higher livestock and feed costs, which resulted in tighter margins for the livestock sector.

These upstream cost increases had a direct impact on food and beverage manufacturers, who were forced to increase prices. Food manufacturing selling prices increased 10.2% in 2022 compared to revenue increasing 12.6%. Beverage manufacturing prices increased 9.1% compared to revenues increasing 0.6%, as alcoholic beverage volumes declined year-over-year.

Farmland values continue to trend higher

Robust farm revenues and low interest rates in the first half of 2022 supported increased land values. Average farmland values increased 12.8% on average. Strong farmland values continue to support producers' balance sheets. More information regarding farmland values, including regional analyses, is available in the FCC Farmland Values Report at fcc.ca/FarmlandValues.

Higher interest rates pushing debt higher and limiting manufacturing investment

Farm debt increased an estimated 8.0% in 2022 with an average annual growth rate of 6.9% over the past 10 years as producers continued to make strategic investments to improve the productivity and efficiency of their farm operations. High costs for both crop inputs and feed increased the demand for short-term debt while higher land values pushed up capital requirements in 2022.

Food and beverage manufacturing capital expenditures as a percent of revenue declined to 2.5% in 2022, the lowest level since 2017. Investment in technology has become more important than ever given the tight labour market. Yet, the effective business borrowing rate doubling year-over-year has made these investments more difficult for producers that are not in a strong financial position

Trade during geopolitical uncertainty

Exports are key to Canada's success as a leading agricultural and food producing nation. With a small population and vast amount of land, we rely heavily on exports. As of 2021, Canada was the fifth-largest exporter of agriculture products and the 11th-largest exporter of food products in the world.

The landscape for world trade presented challenges for the agriculture and agri-food industry in 2022. The war in Ukraine and resulting tariffs significantly limited trade with Russia and Ukraine, while COVID-zero policies in China and the rebuilding of their hog supplies slowed export growth opportunities.

Food and beverage manufacturing margins under pressure

Higher input prices, elevated wages and shifting consumer purchasing patterns towards lower-priced foods in the face of tighter wallets directly impacted food and beverage manufacturing gross margins.

Upstream demand from retailers was also impacted, with 2022 seeing a net closure of food and beverage service establishments. FCC Economics gross margin index in 2022 fell 10% year-over-year. This is the sharpest decline on record. Declines were widespread, except for grain and oilseed milling and meat product manufacturing. Beverage, sugar/chocolate and seafood manufacturing saw the steepest declines.

Current and potential impacts for FCC

The Canadian agriculture and agri-food industry remained financially healthy at the end of 2022 despite margin compression in certain industries. A supportive Canadian dollar and robust global food demand created opportunities for Canadian agriculture, agribusiness and agri-food processors. Global production challenges and strong demand for crops in 2022 resulted in higher prices, supporting the demand for land and farm equipment. Weather, trade concerns, labour availability and higher input prices created numerous challenges, notably for the livestock and horticulture sectors.

Food manufacturing remains a significant driver of the Canadian economy. Small- to medium-sized food processors are delivering innovative food products to Canadians, and larger processing firms are capitalizing on the growing demand for safe, high-quality food in foreign markets. Agriculture, agribusiness and agri-food processors are continually adapting to the changing market environment. Canada's agriculture and agri-food industry has shown resiliency and is well positioned to weather current and future economic hardships and leverage opportunities.

For more information, refer to FCC's sector outlooks at fcc.ca/Economics.

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